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December 12, 2002

<u>BY HAND</u>

Mary L. Cottrell, Secretary
Department of Telecommunications and Energy
One South Station
Boston, MA 02110

Re: <u>Fitchburg Gas and Electric Light Company Request for an Accounting Order</u>

Dear Ms. Cottrell:

Fitchburg Gas and Electric Light Company ("FG&E") hereby seeks approval from the Massachusetts Department of Telecommunications and Energy (the "Department") for an accounting order to mitigate the potential adverse effects on its capitalization, credit quality and borrowing costs resulting from certain accounting requirements related to FG&E's pension plan assets which have been triggered by the substantial decline in the capital markets.

In recent years, the U.S. economy has experienced a significant decline in the equity markets and falling interest rates. This occurrence has had a major impact on FG&E's and other companies' obligations regarding employee pension plans. In the recently concluded base rate cases in DTE 02-24 (gas) and 02-25 (electric), the Department approved new base rates for FG&E which reflected a 2001 test year proformed to include no pension expense. In contrast, FG&E expects to incur a pension expense of over $200,000 in 2003 and make cash contributions to the pension plan. As explained herein, FG&E will also be required to recognize an additional minimum liability. The additional minimum liability will include the excess of the actuarially determined accumulated benefit obligation over the plan assets and a reversal of any previously recorded prepaid pension costs, resulting in a significant reduction in FG&E's equity. By this request, FG&E is seeking an accounting order concerning the potential reduction in equity it may have to recognize at the end of 2002.

Within the past 60 days, FG&E has been notified by its pension plan actuaries that due to the significant decline in the capital markets and lower interest rates, FG&E's estimated year-end pension plan assets, which are held in trust to meet employee pension obligations, would not cover the Plan's Accumulated Benefit Obligation ("ABO") on December 31, 2002. As a result of this unfunded ABO at the year-end measurement date, FG&E will be required to reduce common equity in the amount of $4.6 million (by reversing the prepaid pension cost of $3.9 million and recognizing the current year unfunded ABO of $0.7 million), as prescribed by Financial Accounting Standard Board ("FASB") Statement of Financial Accounting Standards ("SFAS") No. 87, "Employers Accounting for Pensions", and SFAS No. 132, "Employers Disclosures about Pensions and Postretirement Benefits."

The FASB pronouncements require that additional minimum liability be recorded as a non-cash charge to Other Comprehensive Income ("OCI"). Such a charge would not affect the results of operations for 2002. However, the adjustment would require a reduction in FG&E's equity. FG&E's current equity ratio is 34%. The charge to equity would result in a decline in the equity ratio to 31%. This charge to OCI will be reversed in future periods when the value of the plan's assets equals or exceeds the ABO.

FG&E requests permission to record its additional minimum liability, as defined above, as of December 31, 2002 (now estimated to be $4.6 million), as a regulatory asset pursuant to FASB No. 71, in Account 263, pension reserve, with the offsetting charge in prepaid pension expense charged to Account 186. FG&E would perform an annual evaluation of its unfunded status and seeks permission to continue to account for pension obligations as described above in any year in which FG&E's pension plan assets do not exceed its ABO. In addition, when FG&E's plan assets once again exceed its ABO, the Company will notify the Department and will cease recording the regulatory assets and associated remaining liability from its accounts. FG&E will also remove any additional minimum liability, as defined, from its accounts.

Granting the Company's request for an accounting order will allow FG&E to treat its additional minimum liability as a regulatory asset under FASB No. 71 and allow it to avoid the reduction in equity that would otherwise be required by SFAS No. 87. Such an accounting order is appropriate because, under Massachusetts law and Department precedent, a utility's prudently incurred pension obligations are recoverable through rates. Issuance of the accounting order is in the public interest because it will avoid significant pension accounting-related swings in the Company's debt/equity ratios based upon the movements of the capital markets and the resulting negative impact on the Company's capitalization, credit quality, and borrowing costs.

FG&E is not seeking any change to its rates as a result of the requested accounting order. Any such request in future rate proceedings would be subject to review by all parties and approval by the Department. FG&E's recently approved base rates do not recover any pension costs from ratepayers. In contrast, FG&E will begin making significant cash contributions to the pension plan and recording additional pension expenses in 2003 and future periods.

Because of the need for expedited consideration of this matter, FG&E has limited its requests for an accounting order to the treatment of the additional minimum liability as a regulatory asset and is not seeking to defer current pension expense or cash funding being incurred by the Company at this time. However, FG&E may in the future propose a specific ratemaking methodology to recover and reconcile these significant changes in pension costs and will seek the appropriate approvals from the Department.

Because FG&E will need to make provisions for this liability by December 31, 2002, the Company respectfully requests that the Department consider this matter on an expedited basis and approve FG&E's request on or before December 31, 2002.

Very truly yours,

Scott J. Mueller

SJM/va

cc: Paul Afonso, Esquire
Joseph A. Rogers, Assistant Attorney General
Mr. Kevin Brannelly, Director, Rates Division

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